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No. 37

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1936

INTERNATIONAL SHOE COMPANY, Petitioner,

vs.

FEDERAL TRADE COMMISSION, Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

BRIEF FOR PETITIONER.

E 1 Management of properties after stock acquisition P. 19

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1929.

No. 42

INTERNATIONAL SHOE COMPANY, PETITIONER,

vs.

FEDERAL TRADE COMMISSION, RESPONDENT.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

BRIEF FOR PETITIONER.

I.

The opinion of the Circuit Court of Appeals for the First Circuit is reported in 29 Fed. (2d.) 518.

II.

JURISDICTION.

Paragraph 1 of Rule 12 has been complied with in this case and this Court has determined that it has jurisdiction and has granted the Writ of Certiorari (R. 716).

IIa.

The Issue in the Case

This proceeding was brought by the Federal Trade Commission under Section 7 of the Clayton Anti-Trust Act (October 15, 1914; 38 Stat. 730), the first three paragraphs of which are as follows:

> "Sec. 7. No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce.
>
> "No corporation shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of two or more corporations engaged in commerce where the effect of such acquisition, or the use of such stock by the voting or granting of proxies or otherwise, may be to substantially lessen competition between such corporations, or any of them, whose stock or other share capital is so acquired, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce.
>
> "This section shall not apply to corporations purchasing such stock solely for investment and not using the same by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition. Nor shall anything contained in this section prevent a corporation engaged in commerce from causing the formation of subsidiary corporations for the

actual carrying on of their immediate lawful business, or the natural and legitimate branches or extensions thereof, or from owning and holding all or a part of the stock of such subsidiary corporations, when the effect of such formation is not to substantially lessen competition."

The complaint filed May 18, 1923, charges that the International Shoe Company in May, 1921, acquired the share stock of the W. H. McElwain Company, and that the effect of the acquisition was to substantially lessen competition between the two corporations, to restrain commerce, and to tend to create a monopoly, in the shoe business.

The charge of a tendency to monopoly has been abandoned; the complaint stands upon the first two charges and these are restricted to one class of shoes produced by the International Company.

The defense is (a) that there never was substantial competition between the two corporations and that, therefore, the charge of a substantial lessening lacks foundation; (b) that at the time of the acquisition the financial condition of the McElwain Company was so desperate as to necessitate liquidation or sale, and that, therefore, the prospect for future competition or restraint was entirely eliminated.

There is no charge of a design or intent to violate the statute; indeed, it was conceded during the progress of the hearing that the motive prompting the transaction was altogether proper.

There is no conflict in the testimony with respect to the stock acquisition. That testimony is voluminous and exhaustively presents every phase of the case. From this testimony the Federal Trade Commission has drawn inferences and announced conclu-

sions, which, it is respectively submitted, are not warranted.

The authority of this tribunal is invoked to examine the evidence and the method by which the Commission reached its conclusion, and to determine whether, under the undisputed testimony, the findings and the order were justified.

III.

Statement of the Case.

(All record references are to new paging of record according to record printed by the clerk in this Court.)

(A) Parties to the Transaction.

The transaction in question was had in May, 1921.

The parties were: the International Shoe Company, a Delaware corporation, with headquarters at St. Louis and having outstanding preferred stock of the aggregate par value of $12,250,000 and 765,000 shares of common stock of no par value (R. 588); and the W. H. McElwain Shoe Company, a Massachusetts corporation, with headquarters at Boston, and having outstanding capital stock of the par value of about $13,000,000 (R. 224).

There were in 1921 about fifteen hundred other shoe manufacturers in the United States (R. 71). Among these, the International Shoe Company was the largest in respect of the total number of pairs produced of all kinds and varieties. It owned and operated thirty-two shoe factories situated in Missouri, Illinois and Kentucky, with a total daily capacity of 70,000 pairs (R. 520), which represented about 7.34%

of the country's output (R. 200-1). The McElwain Company was among if not the largest in New England. It had factories situated in New Hampshire (R. 214). Its factories had a rated capacity of from 38,000 to 40,000 pairs per day, but in 1921 it was producing only about 6,000 to 7,000 pairs per day (R. 100), representing about 1.33% of the country's output (R. 200-1.) However, it is conceded throughout that the alleged competition involved only men's dress shoes (Commission's Findings, Paragraph 23, R. 532), that is to say welt shoes suitable for street and office wear in contradistinction to work shoes (R. 221). Such shoes constituted the staple of the McElwain Company (R. 215), but only about 4% (or 3,000 pairs per day) of the International Company's output (R. 168, 467). In New England alone there were at least 10 other manufacturers which equalled or exceeded the International Shoe Company in the production of dress shoes for men (R. 466).

(B) The Testimony With Respect to the Existence of Competition in the Sale of Dress Shoes for Men.

In the effort to show the existence of competition the Commission did not call a customer or a salesman of either concern. The only witnesses examined on the issue were the officers of the petitioner, and they testified that there was no substantial competition.

Mr. Rand, President of the International Company, said (R. 60):

> "I cannot recall an instance in which we had McElwain shoes called to our attention in a competitive way, from the standpoint of price or quality."

Mr. Jackson Johnson, Chairman of the Board, said (R. 156):

> "I never felt that there was any competition—that is, what you would call substantial competition. At most it was incidental, and it was so imperceptible that I would not know where to locate it."

The respective products of the two companies differed in selling quality. Mr. Stanley King, who, prior to the acquisition had been an officer of the McElwain Company, and subsequently went with the International Company, concerning the two makes of shoes said (R. 289-90):

> "The McElwain shoes in our opinion had a better finish and workmanship, more attractive and more modern lasts, from the point of view of the city trade, than the shoes of the International Shoe Company, and McElwain used substitutes for leather in its counters, heels and to some extent in its inner soles, as to which the International Shoe Company use no substitutes for leather. Our shoes had, in our opinion, a more attractive finish and appearance and more up to date lasts and patterns."

With reference to this difference Mr. Johnson said (R. 159):

> "My information, and that has come largely since our acquisition of the [McElwain] company, is that they made a line of goods that appealed largely to the city trade. Their construction and finish were of a nature that quite largely appeal to the city buyer, in that they gave a great deal more attention to finish than they did to wearing quality. Our company reversed that. We gave a great deal more attention to the wearing quality of our goods than we did to details

and finish, and that is the differentiation that I would make."

As to the effect of this difference on the sale of the shoes Mr. Johnson testified (R. 168):

> "I think they [i. e. International Company's shoes] were better [i. e. than the McElwain Company's] that is from the standpoint of service, but the unfortunate part of it is we could never convince the retailer who catered to city or dressy wear, we could not convince him of that fact,—the fact that our company travelled five hundred men and we were able to sell only three thousand pairs a day and that would be a maximum I think of our Patriot [i. e. men's dress] shoe."

The trade policies of the two companies differed essentially and in a way that confined the International Company to customers in small towns, while enabling the McElwain Company to meet the demands of the wholesalers and large retailers.

The McElwain Company, when requested so to do, stamped on the shoe the name or brand of the customer; the International Shoe Company refused to do this (R. 290; King).

Concerning the effect of this attitude Mr. Rand said (R. 469):

> "The large retailer in the large cities, who has his shoe store in the best retail streets of the city particularly, insists on advertising his own name, and not the name of the manufacturer. He would not buy shoes from a manufacturer under the manufacturer's name, because of the very sound reason that his overhead cost and expenses are larger and he is unwilling and unable to compete with the man in the outlying districts, with cheaper rent and cheaper property; and, whatever his costs may be, our experience with him has

been a positive refusal to buy our merchandise except under their own names; and we were equally positive in the refusal to put their own names on it, and we did not come together. We are just as far apart as the ocean."

The bulk of the International Company's business was in the south and the west (R. 161, Johnson), while that of the McElwain Company was north of the Ohio River and east of Illinois (R. 218, King).

The International Company sold over 95% of its product in farming communities; in towns having a population of 6,000 or less (R. 162, Johnson). The McElwain Company sold over 95% of its product to jobbers, wholesalers and dealers in towns having a population of 10,000 or more (R. 463, Rand).

During the calendar year preceding May, 1921, the International Company sold to 19 customers of the McElwain Company only 52 5/12 dozen pairs of dress shoes for men (R. 452, Rand).

(C) The Situation in 1921.

Up to 1920 the business of manufacturing shoes was generally prosperous. In the latter part of 1920, and early in 1921, it suffered a serious depression (R. 105, Rand; R. 153, Johnson; R. 290, King).

The experience of the two concerns was precisely opposite. The International Shoe Company adopted a policy of caution; purchased materials conservatively and anticipated the coming depression by slightly lowering its prices (R. 139, Rand). In the spring of 1921 it had orders greatly in excess of the capacity of its factories (R. 152, Johnson). There was not time to erect new factories to meet these orders (R. 40-1, Rand).

The McElwain Company, on the contrary early in 1920, had contracted for an abundant stock of hides and other materials at peak prices (R. 290-1, King). It could not afford to meet the decline which came about. In the summer of 1920 its orders were cancelled to the extent of $7,000,000 (R. 578).

In the early months of 1921 its factories, which had a rated capacity of about 38,000 pairs per day, were producing only about 6,000 or 7,000 pairs (R. 100, Rand). In the course of a year (from May, 1920) a balance sheet surplus of $3,888,440.00 was turned into a deficit of $4,382,136.00 (R. 203-4). It had discontinued the payment of dividends on its second preferred and common stock and was faced with the necessity of discontinuing dividends on the First Preferred shares (R. 579). It owed approximately $15,000,000 to some 67 banks (R. 291, King), and about $2,000,000 on open account (R. 613; Balance Sheet April 30th). Its paper was maturing (R. 349). Its fiscal year ended May 31 (R. 292-3) and the date for publishing its financial statement (required under the laws of Massachusetts) was approaching. Efforts to secure extensions or new capital had been exhausted, and after months of consideration the conclusion was reached by the officers and their financial advisers that the choice was between a liquidation receivership and a sale (R. 294, 350).

The changed situation is made clear by comparing conditions in 1920 and 1921 with respect to (a) production, (b) sales, and (c) working capital.

(a) The production (stated in pairs) during the first five calendar months was as follows (R. 674; Ex. No. 39):

1920	1921	Decrease	% Decrease
3,230,347	932,497	2,297,850	71%

(b) The volume of sales during the first five calendar months was as follows (R. 674; Ex. No. 40):

1920	1921	Decrease	% Decrease
$16,246,941	$3,794,522	$12,452,419	76%

(c) The progressive depletion of its working capital as shown by the balance sheets for May 30, 1920 (R. 655-6), February 28, 1921 (R. 645), April 30, 1921 (R. 613), May 31, 1921 (R. 656-7) and November 30, 1921 (R. 657-8), is here indicated:

	Current Assets	Current Liabilities	Working Capital
May 30, 1920	$26,191,649.45	$12,687,728.82	$13,503,920.63
Feb. 28, 1921	26,894,457.41	17,330,596.89	9,563,860.52
Apr. 30, 1921	21,448,783.64	17,177,349.25	4,271,434.39
May 31, 1921	19,403,715.88	15,880,901.42	3,522,814.46
Nov. 30, 1921	12,735,599.14	13,701,494.37	965,895.23

On May 31, 1920 (R. 655-6) the balance sheet shows a surplus of $3,888,440.73; on April 30, 1921 (R. 613), there is a deficit of $3,425,217.33—a loss in condition during 11 months of $7,313,658.06.

The balance sheet for April 30, 1921 (R. 613) shows current assets of $21,448,783.64, but of this amount $10,275,521.43 included the inventory value of shoes for which there was no sale (customers had cancelled orders to the extent of $7,000,000), customers' accounts represented $8,028,082.41 of its current assets, and it had cash on hand of $2,172,345.16. On April 30, 1921, the company owed in current accounts $1,958,349.25, and in unsecured notes held by 67 banks in New England $15,219,000—a total current indebtedness of $17,177,349.25 (R. 613).

The report of financial condition for 1921 contrasted with that of the year preceding, when filed in obed-

ience to the laws of Massachusetts, would have exhibited these changes:

	Excess of current assets over current liabilities (In round figures)
May 31, 1920	$13,500,000 (R. 655-6)
May 31, 1921	3,523,000 (R. 656-7)
Loss on operations for the year	$ 9,977,000
	Profit and Loss
May 31, 1920—Surplus	$3,888,440 (R. 655-6)
May 31, 1921—Deficit	4,382,136 (R. 656-7)
Loss in condition	$8,270,576

And even so Mr. King testified (R. 313) that the sale of the merchandise and the collection of the receivables disclosed that the condition of the company as of April 30th had been overstated "to the extent of several million dollars."

(D) Conferences Leading Up to the Transaction.

Under these circumstances, in the latter part of March, 1921, the International Shoe Company being without knowledge of the situation, Mr. McElwain, President of the McElwain Company, came to St. Louis without notice (R. 143, Johnson).

Mr. Rand was absent in Mexico. Mr. McElwain saw Mr. Johnson and left without accomplishing anything (R. 143-4).

Mr. McElwain and Mr. King again came to St. Louis about April 8th and submitted a written statement of the condition of the McElwain Company as of February 28th. Mr. Johnson declined to state any definite attitude of the International Company owing to the absence of Mr. Rand, the President (R. 144-5). Mr. McElwain asked when Mr. Rand returned if Mr.

Johnson and Mr. Rand would come to Boston. Mr. Rand returned about April 17th (R. 147). Accordingly late in April Mr. Johnson, Mr. Rand and Mr. Moulton, representing the International Shoe Company, went to Boston and had an interview with Mr. McElwain, Mr. King, representing the McElwain Company, and Mr. James J. Storrow, of Lee, Higginson & Company, representing the first preferred stockholders of the McElwain Company. This discussion extended over three days; it turned about the financial condition of the McElwain Company and resulted in nothing, for the reason that the representatives of the International Shoe Company refused to consider any proposition whatever without an inventory and an audit of the McElwain Company (R. 147-8, Johnson).

Mr. Johnson and Mr. Rand left for New York, where they were followed by Mr. King and had further discussion about the situation without result (R. 148-50, Johnson). Later, about May 8th, Mr. McElwain and Mr. King again came to St. Louis and at that time the agreement which is now under consideration was reached.

In the several conferences discussion was confined solely to assets on the basis of sound value (R. 78, Rand). When tentative agreement of their value was reached, it then became apparent that all the McElwain management and employees who held second preferred and common stock (R. 225, King) would be "broke", as nothing would be left out of the value of the assets to apply to such shares. In explaining to Mr. King why the International Company could not purchase the business on the basis of the inventory, Mr. Rand testified that he said (R. 82):

> "'The principal reason is, the showing is very much worse than we had anticipated, and the

statement shows, after proper deductions from assets, that the common stock is worth less than nothing, and if we secured that company we could not run it from St. Louis, and if we attempted to run it with the association of the men who have been running it, they would all be broke and hopeless, and they could not succeed, and we would not have the company on that basis, because the basis would be unworkable.' Mr. King was necessarily anxious and solicitous about something being done. We then adjourned to my bedroom and then tried to work out some basis for these assets that would express itself in the stock of the company and leave to the management of the company some returns for the efforts of a lifetime; and we did work out some figures on the issue of preferred stock by manipulating those figures so that the various prices for the three types of stock, in round figures, would amount to the same as the value of the company indicated by its inventory figures of April 30th."

(E) The Contract for the Acquisition of Stock.

Accordingly the International Company agreed to buy, and the McElwain Company's executives agreed to sell and cause to be delivered, all shares of all classes of stock for an aggregate sum equivalent to the agreed value of the assets (R. 84-5, Rand), paying 82½% of par for the first preferred, 75% for the second preferred, and 50% for the common. The agreement was executed May 11, 1921, and is set forth (R. 616, *et seq.*).

The avowed purpose was to satisfy all debts, to avoid the serious consequences of a general crash, to secure to the stockholding members of the McElwain organization enough to retain their active interest in reviving the failing concern, and for the International Company to have sufficient factories to meet its re-

quirements. The International Company had no organization in New England and was in no position to man this added enterprise from St. Louis. Concerning this circumstance Mr. Rand said (R. 50-1):

> "We would not have had those properties with all of the management and everyone gone, because we could not run it twelve hundred miles from St. Louis, with the personnel broken down, hopeless, and with new men—we did not have a surplus of men in our organization here in St. Louis to go down and direct the manufacture and distribution of 40,000 pairs of shoes additional. We needed help. We needed intelligent, loyal help; and that was the one reason why we positively declined, at any price, to buy for cash the physical assets of the company and disregard the entire organization."

The contract called for the delivery of *all* shares (R. 616). Thirty-five shares of First Preferred and fifty shares of Common failed to come in (R. 104), and this was what delayed the formal acquisition of the assets by the International Shoe Company (R. 103, 120). The rest came in promptly upon the representation by officers of the McElwain Company of the actual situation.

The contract of sale contained no restriction as to the right of any members of the McElwain Company to engage in the business of manufacturing shoes (R. 100), as a number of them have since done.

Lee, Higginson & Co., of Boston, who had placed the preferred stock with their customers, advised the sale as the best thing that could be done under the circumstances, in the following language:

> "We approve of the above agreement, and agree to use our best efforts to secure the accep-

tance of it by the holders of the first preferred stock of W. H. McElwain Company.

Lee, Higginson & Co." (R. 619.)

Mr. Rand, referring to what took place at the final conference before the contract of purchase was agreed upon, said (R. 83):

> "We discussed and discussed that [i. e., the financial condition of the McElwain Company], with Mr. King and Mr. McElwain and all of us were conscious of the fact that the company in this financial condition, with a liability on April 30th of $17,177,000, could not keep its doors open thirty days longer."

Mr. Johnson testified that at the conclusion of a conference in Boston in the latter part of April, he told the executives of the McElwain Company that they were "broke" (R. 148).

Mr. King described the situation in the following language (R. 300):

> "Mr. Storrow was unwilling to agree to the suggestions which had been tentatively agreed upon between the representatives of the International Shoe Company and the McElwain Company, on the ground that it did not adequately compensate the first preferred stockholders. I advised Mr. Storrow that it was essential that he agree, because in addition to the financial condition of the company, with which he was familiar, the management of the company was on the edge of a breakdown; Mr. McElwain had already broken down two days before. The first vice-president of the company had broken down two months before; the treasurer of the company had given up his major responsibilities eight months before, and the second vice-president of the company was on the edge of a breakdown and the company would disintegrate and the management

would disintegrate physically unless the situation was saved at once. Mr. Storrow then agreed. A contract was drawn and signed."

Mr. King further testified (R. 293-4):

"The financial condition of the McElwain Company at that time [to-wit, April 5, 1921] was practically insolvent, and in my opinion at that time, which I still hold, the company would have been actually insolvent upon the publication of those figures."

Ernest S. Gile, publisher of the Weekly Bulletin of Leather and Shoe News, testified (R. 363) that there was no criticism from a standpoint of injury either to the competitive shoe manufacturers, or to the supply houses and leather trade who sell the manufacturers. That the approval had been general, and that he had gone into that question thoroughly.

Mr. William A. Copeland, President of the General Shoe Machinery Company, testified as follows (R. 369):

"I understood about that time [i. e. about May 1921] that they were in financial difficulty, and that if they did not receive help that they would have to go into the hands of a receiver."

Asked (R. 376) whether his estimate as to the situation was not purely speculative, witness answered:

"If you asked what the effect would have been if the McElwain Company had gone into the hands of a receiver, I don't think there is such [much] speculation as to that effect."

Asked again (R. 377):

"I understood you to be basing your answer on what would have happened if the International Shoe Company had not acquired the stock of the W. H. McElwain Company."

To which the witness answered:

> "Almost synonymous, aren't they? Who else would have acquired it, if the International Shoe Company had not? The banks would have had to close them out, and you know what the effect of closing out of a large shoe industry, with all the factories centered within a few miles of each other, is."

The McElwain Company owed the First National Bank of Boston $1,000,000 (R. 352). Clifton H. Dwinnell, Vice-President of the bank and who for years had been in charge of leather and shoe credits, testified (R. 349) that he was familiar with the financial condition of the W. H. McElwain Company, and that it was very critical; that after discussions with representatives, he had told them that something had to be done right away or they would be in trouble.

In answer to Mr. McElwain's question whether it would be advisable for him to ask for extensions from his banks, witness told him that he might ask, but he could not answer as to that.

The advisability of getting more capital or selling out was discussed. As to capital, McElwain said it could not be done.

The suggestion of additional capital had been discussed with Lee, Higginson & Co., who had put out some of the securities of the McElwain Company. Witness further answered that the extension could be tried, but he felt it really was impossible, because there were so many banks involved, and that a receivership or sale was the only alternative.

As to the attitude of the Bank with respect to the $1,000,000 owing to it, Mr. Dwinnell said (R. 354):

"I can say this; that it was our intention to ask the McElwain Company to pay its loan; that had been gone over by our executive committee."

Asked what would have been the result of a receivership, he answered that he doubted whether stockholders would have had anything at all.

In answer to the question what would have been the result as to the communities its factories were located in, he answered (R. 351):

"Well, I think the—of course a lot of people would have been thrown out of employment; but what concerned me more was its effect on the other shoe industries in New England, as far as their credit was concerned."

Continuing:

"I think it would have caused a lot of distress to the other manufacturing concerns, because the failure of W. H. McElwain Company would have been almost the last straw; and in a time like the spring of 1921, probably banks, in a great many cases, would have called their shoe and leather notes."

Continuing:

"I think the shoe and leather and hides have been so closely allied, that it would have had a bad effect on the standing of those other kindred lines, as well as the shoe lines, from a credit standpoint."

Asked what was the result of the sale to the International Shoe Company, the answer was:

"I think it averted a catastrophe for New England; incidentally resulted in the payment of $15,000,000 or $16,000,000 worth of debts."

There is nothing in the testimony to indicate that the

E 1, Management & control of properties after stock acquisition by International Shoe Co.

International Shoe Company had in any manner influenced or helped to bring about the dilemma in which the McElwain Company found itself; or, indeed, had any information about the situation until they were called upon for assistance.

Upon the consummation of the sale in May, 1921, the International Shoe Company broadly advertised the transaction, particularly in the East. It at once sold some of the distributing branches of the McElwain Company to the managers of such branches; it tried to sell the others and after failing to do so, closed them to save further loss (R. 303, King). It reduced the prices of the shoes on hand and sold them as rapidly as possible (R. 173); it endeavored to collect accounts, but did so with heavy losses (R. 313); it operated all factories, giving work to all old employees and maintaining the full wage scale (R. 176).

Between May 11th and November 30th, the International Shoe Company advanced the McElwain Company $11,850,000 to pay its maturing debts (R. 197), which could not have been satisfied otherwise even measurably without a sale of the McElwain factories.

The International Shoe Company used the newly acquired factories to manufacture its own kind of shoes to meet its particular needs. It converted some of the factories to the production of shoes for women, and others into producing girls' shoes. The factories as a whole were used to make a general line of shoes rather than men's dress shoes only. However, it continued to produce such shoes according to its own specifications (R. 39).

With the factories so transformed, the International Shoe Company increased the output (R. 674; Ex. 39,

showing production in pairs monthly from 1920 to 1924).

Between the date of the acquisition (May 11th) and the end of 1921 the western branches of the International Shoe Company ordered from the McElwain factories 794,000 pairs. During 1922 the International Shoe Company took 58% of the total output, and during 1923 56% (R. 196).

Throughout the purchasing company treated the property of the selling company as part of its own system, although the paper organization of the McElwain Company was retained until some time in June, 1923, and records were kept separately of its financial condition.

On May 18, 1923, two years after the purchase, the facts having been public property during the intervening period, the Federal Trade Commission filed its complaint (R. 21).

In the meantime, several of the stockholders and officers of the McElwain Company had again engaged in the business of manufacturing shoes, and were, when the proofs were taken in June, 1924, pursuing that business (R. 304, *et seq.*). The International Shoe Company, however, having paid all the debts of the McElwain Company, having provided the necessary capital for operating the factories, having re-employed its entire force at regular wages, and having produced a larger output of shoes than had been done in the year preceding the acquistion, sustained a loss of more than $4,000,000. For all shares of all classes of McElwain stock (including 69,946 First Preferred Shares, R. 192) the International Shoe Company paid $9,460,000 (R. 193). Mr. Gray, auditor for the Company, testified that this was over twice the real value; that

when the entire net worth of the Company as of November 31, 1921, is allocated to the First Preferred shares, it gives a value of $57.01 per share (which is equivalent to about $4,000,000 for 69,946 shares) leaving no value to the second preferred and common stock (R. 206).

Immediately after the complaint was filed, the International Shoe Company divested itself of the paper title to the shares of stock in the McElwain Company and acquired the technical title to the assets (R. 49-50). The International Shoe Company, by the employment of the facilities of the McElwain Company, was enabled largely to fill its own orders. Since then the plants have been actively operated continuously, but with every financial support they have not been operated with profit.

(F) The Findings and Order of the Commission.

The Commission made an elaborate written report (R. 519-42) in which (a bare majority concurring) it found that (R. 522) "on and prior to May 11, 1921" * * * "the competition in commerce between the two companies was substantial"; that (R. 532) the effect of the acquisition was (a) to substantially lessen competition between the two concerns "in the sale of dress shoes for men"; (b) to restrain commerce in the sale of such shoes. The charge that the acquisition had a tendency to create in petitioner a monopoly in the shoe business was dropped and is out of the case. As to the defense based upon the insolvent condition of the McElwain Company, the Commission found that (R. 532-3) at the date of the stock acquisition the McElwain Company was not insolvent within the meaning of the National Bankruptcy Act.

By its order (R. 542), the effective date of which is May 7, 1927 (R. 559), the Commission called upon the petitioner to divest itself of the stock of the McElwain Company and to cease and desist from the ownership, operation and management of the properties formerly owned by the McElwain Company.

Commissioners Hunt and Humphrey dissented. Commissioner Humphrey filed a memorandum of dissent, concurred in by Commissioner Hunt, which is in part as follows (R. 544 et seq.):

> "In this case the evidence shows the following facts:
>
> 1. That the respondent acquired the stock of the McElwain Company.
>
> 2. That the respondent and the McElwain Company at the time were in competition. Whether such competition was material, is a matter of opinion.
>
> 3. That the McElwain Company initiated the transaction.
>
> 4. That at the time of the transaction the McElwain Company was in a failing financial condition, or at least its officers believed that it was, and they believed that its bankruptcy was probable.
>
> 5. That the respondent at the time had taken more orders than it was able to fill, at its then capacity, and was considerably troubled with these excess orders, and was very desirous, for this reason, of increasing production.
>
> 6. That it used the organization and assets acquired from the McElwain Company in increasing its output, largely for the purpose of filling these excess orders.
>
> 7. That the respondent did not increase prices; on the contrary, in some instances, it voluntarily decreased prices.
>
> 8. That it made better shoes, and sold them for the same or less money than the McElwain Com-

pany was selling the same class of shoes at the time the respondent acquired its stock.

9. That the respondent did not use the stock so acquired by voting or otherwise to bring about, or attempting to bring about, the substantial lessening of competition.

10. That the public was in no degree, in any way, injured by the transaction. On the contrary, the evidence shows that the public was benefited thereby.

QUESTIONS OF LAW.

"Admitting, but not asserting, that there was substantial competition between the respondent and the McElwain Company at the time of the transaction complained of, it was probable that this competition was going to be destroyed by the failure of the McElwain Company. This circumstance removed the very evil that the statute was intended to prevent. This being true, the transaction was not unlawful (*American Press Association v. United States*, 245 Fed. 91)."

* * * *

"Had the respondent been content to wait, if we are to be guided by the evidence, then in a short time its competitor would have been bankrupt. The stockholders would have lost their entire investments. A great organization would have been destroyed and the competition with which the respondent is charged with destroying would have been wiped out without cost to the respondent of a dollar.

"In this case, the commission has given warning to the business world that no one must answer the cry of distress. If they do, and save a vessel from complete wreck, no matter what the effect may be upon the public, they will be condemned and must suffer the penalty. But it will be perfectly proper and commendable to stand by until the vessel sinks, and its competition with them is thereby entirely destroyed, and then pick up whatever flot-

sam and jetsam they may, but under no circumstances must the vessel be saved, however much it may be to the public interest. I think such policy must inevitably injure the public and be immeasurably detrimental to our industries.

"I can not be oblivious to the fact that by the issuance of this order many innocent investors will be injured and that no one will be benefited."

In its efforts to show the Commission that its order could not be complied with, petitioner finally moved the Commission for leave to take further testimony (R. 26), and to have it modify its order. To that end petitioner alleged and offered to prove (R. 28) that the properties formerly belonging to the McElwain Company can not be sold for any reasonable price to a responsible purchaser who can and will continue the production of shoes; that without the capital, merchandise orders and trade supervision of the petitioner, investors can not be induced to embark capital in the business formerly conducted by the McElwain Company. The Commission ignored the motion and the offer of proof.

(G) The Decision of the Court of Appeals.

On March 3, 1928, petitioner filed its petition (R. 1) to have the order of the Commission reviewed and set aside. It specifically alleged the insufficiency of the complaint (R. 11), the undisputed proof of the insolvency of the McElwain Company (R. 13), and the positive proof that there was no substantial competition between the two concerns (R. 16).

Petitioner further filed a motion (R. 695) to have the Court of Appeals adjudge the complaint insufficient. The Court denied the motion without comment on the day it was argued (R. 715). The case was heard on the

merits October 4 and 5, 1928, and on November 27, 1928 (R. 715), the Court of Appeals affirmed the order of the Commission, holding that there was substantial competition between the two corporations, and that the McElwain Company was not insolvent (applying the bankruptcy definition of insolvency).

IV.

Specification of Errors

It is submitted that the Court below erred:

(1) In failing to sustain petitioner's motion to dismiss the proceeding because of the insufficiency of the Commission's complaint.

(2) In holding itself bound by the findings of the Federal Trade Commission as to the existence of substantial competition, which are based upon inferences and not upon the evidence.

(3) In sustaining the finding of the Federal Trade Commission that there was evidence of substantial competition between the two corporations at the date of the stock acquisition.

(4) In failing to hold that in contemplation of law the insolvency of the McElwain Company put an end to its ability to compete with anyone.

(5) In applying the Bankruptcy Act definition of insolvency as decisive of the McElwain Company's ability to continue in business and to engage in future competition, and in finding that it was in fact capable of continuing business.

In ignoring the insolvency definition of the Massachusetts law under which the status of the McElwain Company would have been fixed; and in ignoring the crippled financial and commercial condition of the Company as conclusive of the question at issue.

(6) In failing to hold that Section 7 of the Clayton Act has no application to an acquisition of share capital where that step offers the selling company the only escape from liquidation, and the buying company is endeavoring to increase its facilities for output.

(7) In disregarding throughout the undisputed and decisive facts that the purchase of the share capital was not had, and the share stock was not used, to lessen competition, but that the object, intent and purpose of both seller and purchaser was to save a large factory for the protection of creditors and stockholders and the trade.

(8) In disregarding the controlling decisions of this Court and the Circuit Court of Appeals construing the Clayton Act.

V.

Summary of Argument.

(1) The complaint is insufficient. If, for its vague conclusions, a statement of facts that induced the transaction is substituted, it is obvious that there was no grievance to be corrected.

(2) The Circuit Court of Appeals affirmed the order of the Federal Trade Commission on the erroneous theory that its findings, even though drawn from the inferences and not evidence, were binding on the Court, and that it could not, after an examination of the evidence, determine that it did not support such findings or justify the order of the Commission.

(3) There is no evidence of substantial competition at the time of the transaction; hence no basis for the order.

(4) The decision of the Court of Appeals in this

case is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit, affirmed by this Court, construing and applying Section 7.

(5) The evidence is conclusive that the financial condition of the McElwain Company at the time of the transaction was such that it had to sell or liquidate; hence its activities as a shoe manufacturer were ended.

(6) The condemnation of plaintiff in error is grounded upon the Bankruptcy definition of insolvency. That test is irrelevant to the proceeding. The true test is the actual financial condition of the seller.

(7) Section 7 of the Clayton Act has no application to the acquisition by one corporation of the stock of an insolvent corporation, where on the part of the seller the transaction is the only escape from liquidation.

(8) The complaint was purely technical at its inception. Immediately after the complaint was filed plaintiff in error divested itself of the shares. Even the technical complaint was thereby met. While the stock of the McElwain Company was held by plaintiff in error, it was in no sense used to control, lessen, or in any fashion affect, competition in trade; and today no order of the Commission can be made effective beyond what has already been done, because there is no sale for the assets which the plaintiff in error has acquired.

VI.

ARGUMENT.

(1) The Complaint Is Insufficient.

The requisites of a complaint by the Commission when proceeding under authority of the Clayton Act

are the same as when it proceeds under the Federal Trade Commission Act. Paragraph 2 of Section 11 of the Clayton Act (prescribing the essentials of a complaint) is a rescript of Paragraph 3 of Section 5 of the Federal Trade Commission Act. In *Federal Trade Commission v. Gratz,* 253 U. S. 421, which was a proceeding under the Federal Trade Commission Act charging "unfair competition", this Court held the complaint insufficient and declined to review the evidence on which the Commission and the Court of Appeals had acted. The court said (page 427):

> "If, when liberally construed, the complaint is plainly insufficient to show unfair competition within the proper meaning of these words, there is no foundation for an order to desist,—the thing which may be prohibited is the method of competition specified in the complaint. Such an order should follow the complaint; otherwise it is improvident, and, when challenged, will be annulled by the court."

Section 7 prohibits stock acquisitions only *"where* the effect * * * may be to substantially lessen competion", etc. The conjunction "where" requires an allegation of facts constitutive of the forbidden "effect". Waiving technical niceties of pleading and granting that the complaint is to be liberally construed, yet the irreducible minimum is an allegation of facts showing (a) the existence of competition—not "in the shoe business", but—in the sale of a specified class of shoes; and (b) that such competition was substantially lessened—not by reason of some circumstance with which petitioner was in no wise connected, viz., the financial breakdown of the seller, but—as the effect of the stock acquisition by petitioner. Here the complaint is lacking in both respects.

As to the petitioner the complaint alleges (R. 21):

> "The respondent owns and operates thirty-two or more shoe factories in the States of Illinois, Missouri and Kentucky, some of which have been acquired by absorbing competing companies. The respondent also owns and operates stores, selling departments and branch establishments among the several States and the District of Columbia and is and has been engaged in the business of manufacturing shoes for *men, women, boys, children* and *infants,* and in selling *such shoes* to wholesale and retail shoe dealers and other purchasers in the various States of the United States in addition to those States in which its said factories are located."

As to the McElwain Company the complaint alleges (R. 22):

> "It owns and operates shoe manufacturing plants in the State of New Hampshire where shoes for *men* and *boys* have been made and are manufactured and owns and operates stores, selling departments and branch establishments in the cities of Boston, Massachusetts; New York City, New York; Columbus, Ohio; Chicago, Illinois; Kansas City, Missouri; San Francisco, California, and in other places within the several states of the United States and the District of Columbia. It was and is engaged in the business of selling *such shoes* to wholesalers, retailers and others among the several States of the United States, the territories thereof", etc.

As to the existence of competition between the two corporations the complaint alleges (R. 22-3):

> "On and prior to May 11, 1921, the respondent and the said W. H. McElwain Company were in competition with each other *in the shoe business as hereinabove described*".

The complaint does not charge what was the approximate volume of business done periodically by either concern; what quantity, quality or variety of shoes, or at what range of prices, were sold by either; with respect to what kind of shoes there was competition, under what circumstances petitioner acquired the stock; what was the object, purpose and intent of either purchaser or seller; in what respect or degree, and as to what class of shoes, the stock acquisition restrained commerce; in what manner and to what extent the stock acquisition had a tendency to create an unlawful monopoly in petitioner.

(2) The Court of Appeals erred in holding itself bound by the unsupported findings of the Federal Trade Commission.

The Court of Appeals, in holding its jurisdiction did not permit it to go behind the findings of the Commission based on inferences (contradicted by evidence and not justified thereby), has overlooked its province and duty as stated by this Court in *Federal Trade Commission v. Curtis Publishing Co.*, 260 U. S., at page 580, where it says:

> "Manifestly, the court must inquire whether the Commission's findings of fact are supported by evidence. If so supported, they are conclusive. But, as the statute grants jurisdiction to make and enter, upon the pleadings, testimony, and proceedings, a decree affirming, modifying, or setting aside an order, the court must also have power to examine the whole record and ascertain for itself the issues presented, and whether there are material facts not reported by the commission. If there be substantial evidence relating to such facts from which different conclusions reasonably may be drawn, the matter may be and ordinarily, we think, should be, remanded to the commission,—

the primary fact-finding body,—with direction to make additional findings; but if, from all the circumstances, it clearly appears that, in the interest of justice, the controversy should be decided without further delay, the court has full power under the statutes so to do. The language of the statute is broad, and confers power of review not found in the Interstate Commerce Act."

(3) There Was No Substantial Competition.

The Federal Trade Commission's conclusion, that the sale of shares had the effect to lessen competition between the two corporations, is not supported by the testimony.

As to the alleged competition the Commission's Finding (Par. 5, R. 522), which is quoted and approved by the Court of Appeals without any analysis of the testimony, is an inference which is wholly unwarranted by the undisputed facts.

The finding is that the petitioner sold men's dress shoes *"similar in style,* comparable in price and *equal or superior in quality* to the men's high and low dress shoes produced by the McElwain Company." And "Both companies made and sold *medium priced dress shoes* and sold such shoes to retail dealers *in the same States, and in many of the same cities* and towns, and *in some instances to the same dealers."* All these generalities are consistent with the absence of substantial competition and altogether insufficient to show it. The only witnesses who were examined as to competition testified positively and without contradiction that there was no substantial competition.

The record shows that by "similar in style" is meant that both concerns made high shoes and low cuts (R. 340). With respect to quality Mr. Johnson testified, as

we have shown, that the International Company's shoes were not acceptable to buyers and wearers in the larger centers of population.

Substantial competition is a fact, susceptible of direct proof;—it does not rest on inferences. The fact that two manufacturers make men's dress shoes, one as its sole product, the other a small part of its output; —where the shoes are differently constructed and sold to different classes of customers, largely in different classes of towns, does not prove competition, even though during a year nineteen merchants in the United States purchase small quantities of shoes from both manufacturers.

Both the Commission and the Court of Appeals ignore this absence of testimony and these facts which are undisputed.

The Clayton Act names specific grounds of complaint, but its general purpose is that of the original anti-trust statute.

The title of the Clayton Act is "An Act to Supplement *Existing Laws* Against Unlawful Restraints and Monopolies and for other Purposes." The enacting clause provides that the words "anti-trust laws" include the Sherman Act. The statute, therefore, is an amendment of the Sherman Anti-trust Act and should be construed and given effect to as such.

In *United States v. Freeman* (1845), 3 How. 556, 564, this Court said:

> "The correct rule of interpretation is, that if divers statutes relate to the same thing, they ought all to be taken into consideration in construing any one of them, and it is an established rule of law, that all acts *in pari materia* are to be taken together, as if they were one law."

Applying this rule of construction, the Court of Appeals for the Third Circuit, in *Standard Oil Company v. Federal Trade Commission* (1922), 282 Fed. 81, 87, said:

> "Though differing somewhat from other laws, as we have indicated, the Clayton Act, nevertheless, deals with matters within the realm of monopoly. Therefore in determining whether given acts amount to unfair methods of competition within the meaning of the Federal Trade Commission Act, or substantially lessen competition and tend to create a monopoly within the meaning of the Clayton Act, the only standard of legality with which we are acquainted is the standard established by the Sherman Act in the words 'restraint of trade or commerce' and 'monopolize or attempt to monopolize' and by the courts in construing the Sherman Act with reference to acts 'which operate to the prejudice of the public interest by unduly restricting competition or unduly obstructing the due course of trade' and 'restrict the common liberty to engage therein.' *Great Atlantic & Pacific Tea Co. v. Cream of Wheat Co.*, 224 Fed. 566, 573; affirmed 227 Fed. 46; *United States v. American Tobacco Co.*, 221 U. S. 106, 179; *United States v. Patten*, 226 U. S. 525, 541; *Eastern States Lumber Asso. v. United States*, 234 U. S. 600, 613, 614; *Standard Oil Case*, 221 U. S. 1; *Standard Fashion Co. v. Magrane-Houston Company*" (258 U. S. 346).

And in affirming the decision of the Court of Appeals (*Federal Trade Commission v. Standard Oil Company*, 261 U. S. 463), this Court said, at page 476:

> "The great purpose of both statutes [i. e. the Federal Trade Commission Act and the Clayton Act] was to advance the public interest by securing fair opportunity for the play of the con-

> tending forces ordinarily engendered by an honest desire for gain."

This is likewise the "great purpose" of the Sherman law.

Both enactments are an exercise of the power of Congress to regulate interstate commerce. In construing the Sherman Act this Court has held that the extent and also the limitations of the prohibitions are measured by consideration of the public interest in interstate and foreign commerce.

Thus in *United States v. American Tobacco Co.*, 221 U. S. 106, 181, the Court, referring to the Standard Oil Case and declaring the extent of the prohibitions, said, "it was pointed out that the generic designation of the 1st and 2d sections of the [Sherman] law, when taken together, embraced every conceivable act which could possibly come within the spirit or purpose of the prohibitions of the law, without regard to the garb in which such acts were clothed".

In the same case, in declaring the limitation of the prohibitions, the Court said (pages 179-180):

> "the words 'restraint of trade' should be given a meaning which would not destroy the individual right to contract, and render difficult, if not impossible, any movement of trade in the channels of interstate commerce,—the free movement of which it was the purpose of the statute to protect".

Earlier in the opinion (page 179), and referring to the opinion in the Standard Oil Case, the court said:

> "It was therefore pointed out that the statute [i. e. Sherman Act] did not forbid or restrain the power to make normal and usual contracts to further trade by resorting to all normal methods,

whether by agreement or otherwise, to accomplish such purpose".

In *Nash v. United States*, 229 U. S. 373, 376, the Court re-iterated the limitations of the prohibitions of the Sherman Act. In summarizing the effect of the Standard Oil and American Tobacco Company cases, it said:

> "Those cases may be taken to have established that only such contracts and combinations are within the [Sherman Anti-Trust] act, as by reason of intent or the inherent nature of the contemplated acts prejudice the public interests by unduly restricting competition or unduly obstructing the course of trade."

In determining whether a given contract or act comes within the scope of the prohibitions, the paramount and decisive consideration is protection of the public interest in relation to interstate and foreign trade. If such contracts or acquisitions have the effect of unduly restricting the course of interstate trade, they are unlawful regardless of the form of the transactions. But if such contracts or acquisitions do not prejudice the public interest in interstate commerce, they do not come within the prohibitions of the Sherman Act regardless of the form of the transaction.

The same limitation must obtain with reference to the specific prohibitions of Section 7 of the Clayton Act, otherwise by that section Congress has prohibited such transactions without regard to the public interest committed to it under the Constitution, that is regardless of the beneficial or harmful effect of such transactions on the course of interstate trade. Such a construction of the Clayton Act, a supplement to

the Sherman Act, would be in direct conflict with the established construction of the Sherman Act, in that under the Sherman Act protection to the public interest marks both the extent and limitation of the power exerted, while under Section 7 of the Clayton Act such public interest would not measure either the extent or limitation of the power exerted. The reason and necessity for limiting the generic prohibitions of the Sherman Act obtain with respect to the specific prohibitions of the Clayton Act. The requirement that the acquisition of shares, and the manner in which the authority so gained is employed, shall have the effect to substantially lessen competition, is directed to the protection of the public interest, just as the provisions of the Sherman Anti-trust Act are. Not a technical, but an actual injury is necessary. The Clayton Act does not impose a penalty upon the person, but makes provision for the substantial protection of the public.

The competition, however, between these two corporations was so remote and so infinitesimal that the effect of its discontinuance upon the public would be purely speculative. Only four percent of the output of the International Shoe Company came in competition with the McElwain Company's product even remotely.

Throughout the quality of materials, the kind of shoes, the method of distribution, the size of towns and the general territory covered, differed essentially. There was no phase of competition between these two companies that was not as completely, if not more effectively, covered by other manufacturers among the fifteen hundred who were then active in business. For these reasons the transaction did not lessen competition.

(4) The decision of the Circuit Court of Appeals in this case is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the case of *Federal Trade Commission v. Thatcher Manufacturing Company,* which Court, in 5 Fed. (2nd) at page 622, paragraphs 6, 7, said:

> "Not every acquisition by one corporation of the stock of a competing corporation is forbidden by Section 7 of the Clayton Act. The act, by express terms, says that Section 7 does not apply to a corporation 'purchasing such stock * * * and not using the same to bring about, or in attempting to bring about, the substantial lessening of competition'. Testing the transaction (as it affected the Woodbury Company) by the whole of Section 7, the evidence discloses that before the respondent acquired the stock of the Woodbury Company that corporation was engaged chiefly in the manufacture of condiment and whisky bottles, and that its manufacture of milk bottles was very small, amounting annually to about 8,000 gross out of a total production in the United States of over one million gross. The evidence also shows that it was gradually getting out of the milk-bottle business and that, indeed, before the transaction in question arose, it had determined to do so. When its stock was acquired the respondent took over its outstanding contracts, one or two in number, and filled them. The respondent's real object in acquiring the Woodbury stock, as we see it, was to acquire its patent license, that being a nonexclusive license to use the Hartford-Fairmont feeders in the manufacture of condiment bottles, fruit juice bottles, fruit containers, fruit jars and glassware for carbonated soft drinks, branches of the glassware business in which the respondent was not engaged, and, therefore, in which it was not a competitor. While the effect of the transaction upon the Woodbury Company was to stop its manufacture of milk

bottles and, accordingly, to end its competition in milk-bottle manufacture, the number of milk bottles the Woodbury Company made was so inconsiderable that the lessening of competition thereby was not substantial. We are, therefore, of opinion that the evidence does not sustain the Commission's finding that the respondent's acquisition of the stock of the Woodbury Glass Company substantially lessened competition between the corporations, restrained commerce and tended to create a monopoly. That part of the Commission's order is, therefore, not approved and will not be enforced."

With reference to that holding this Court in *Thatcher Manufacturing Company v. Federal Trade Commission*, 272 U. S. 554, at 560, said:

> "The court below held that the last named company (i. e. Woodbury Glass Company) was not in competition with petitioner within the meaning of the statute and modified the order accordingly. Therein we agree and to that extent affirm its decree."

The Court of Appeals in the case at bar says that the Sherman Act and the Clayton Act provide different tests of liability (*United Shoe Machinery Co. v. United States*, 258 U. S. 451, 459). While this is true, the Clayton Act does not change the meaning of the terms "substantial competition", "restraint of trade" and "monopoly".

Further, the existence of substantial competition is a necessary condition of liability under each statute, and the absence of such competition here, and the insolvency of the McElwain Company, render both enactments inapplicable. On this ground we submit the decision of the Court of Appeals is in conflict with the principles laid down in cases under the Sherman Act.

In the case of *Standard Fashion Co. v. Magrane-Houston Co.*, 258 U. S. 346, the Court said, at 356-7:

> "Section 3 condemns sales or agreements where the effect of such sale or contract of sale 'may' be to substantially lessen competition or tend to create monopoly. It thus deals with consequences to follow the making of the restrictive covenant limiting the right of the purchaser to deal in the goods of the seller only. But we do not think that the purpose in using the word 'may' was to prohibit the mere possibility of the consequences described. It was intended to prevent such agreements as would under the circumstances disclosed probably lessen competition or create an actual tendency to monopoly. That it was not intended to reach every remote lessening of competition is shown in the requirement that such lessening must be substantial."

The cases of *Federal Trade Commission v. Western Meat Co.*, (272 U. S. 554), and the case of *Aluminum Company v. Federal Trade Commission* (284 Fed. 401) are not in conflict with these decisions, because in the first case the existence of substantial competition by a going concern was undisputed, and while in the Aluminum case the selling company appeared to be in failing condition, the fact is clear that this company was the sole competitor in the field, and that its embarrassment was in large measure attributed to a contract which enabled the Aluminum Company to exert pressure upon it.

(5) But apart from the relation of the state of competition between the two corporations in the past, all chance for competition, present or prospective, was eliminated by the financial dilemma in which the McElwain Company found itself early in 1921. This con-

dition appears from its financial statements, which show a large stock at peak prices, cancellation of orders, curtailment of production by 75%, and a change from a surplus to a substantial deficit in the course of six months, with an indebtedness to 67 banks of 15 million dollars, with no prospect of an extension and with a failure of every effort to secure additional capital.

This evidence is confirmed by the demoralization of practically the entire executive body of the corporation as described by Stanley King. The decision reached by the management reluctantly after months of consideration, is endorsed by bankers and creditors who were vitally interested in the particular and in the general trade conditions, and, above all, by Lee, Higginson & Co., who were the backers of preferred stock, and who were concerned not only in its monetary value, but also in the integrity and wisdom of putting out the preferred stock of this concern.

To hold that the McElwain Company was obliged under these circumstances to continue its business, and to risk the fate of its capital and its creditors upon so doubtful an enterprise, would mean a sacrifice of private property to public policy. The statute undertakes to regulate going concerns; not to determine how the wreckage of a failing concern shall be employed. If a reorganization had been had, or if a receiver had been named, as has been suggested in this case by the Court of Appeals, neither investors nor the Court would have been concerned with the question of how the product of the factories should be sold. If the Court had ordered a sale by receivers or bankruptcy proceedings, the decree would not have contained a provision that the property purchased at such a sale should thereafter pursue its former competitive lines.

When, therefore, the probability of a receivership was apparent, it became the obvious duty of the directors to anticipate that danger and to exercise their best judgement for the preservation of the assets to protect the creditors and stockholders.

There is no question here of good faith. It is admitted that throughout the negotiations the motives of both parties were of the best. Neither is there challenge by a single witness of the soundness of the judgment in making the sale. The officers and directors of the McElwain Company were men of large experience. They had piloted the concern through many years, in good times and bad. Bankers, creditors and independent observers were of one mind, that the sale was necessary, and that the escape from a receivership avoided a general crash and gave protection to creditors and stockholders that no other step could have secured.

The Commission does not attempt to suggest how the Company could have continued its business, but the Court of Appeals says there were "several alternatives", of which three are stated:

> "(a) The McElwain Company's bank creditors might have carried the concern, just as at that time the banks were carrying a very large percentage of the business concerns in this community. It was a period of 'frozen credits,' a time when there was practically a conceded moratorium to a large share of our business concerns, which competed fiercely for rehabilitating trade.
>
> (b) If a receivership had been found a necessary expedient, competition under receivership management would have been likely to be intensified, not eliminated.
>
> (c) In case of actual bankruptcy, the holders of the preferred stock (one or both classes) would in their own interest have taken over the property,

kept it in active operation and therefore in competition."

Each alternative stated by the Court presupposes the inability of the Company to pay its debts as they became due; and the tenability of each alternative is tested by the facts shown of record.

As to (a) the First National Bank of Boston, holding the Company's notes in the amount of $1,000,000, was unwilling to renew or extend them. While the representatives of the other banks did not testify, no doubt the banks were in accord on the matter, for in President McElwain's letter to the shareholders, recommending the sale (R. 579), he said: "While our banks have not yet restricted our credits, we realize that it is not the function of the banks to supply permanent working capital and that the duty and the necessity has rested upon us to reduce our bank loans as rapidly as possible until they come within the compass of our reduced resources." That the banks exacted payment shortly is indicated by the fact that between May 11 and May 31, 1921, the International Shoe Company had to advance $900,000; in the month of June $4,400,000 additional, and that by November 30, 1921, it had advanced over $11,000,000 to meet the debts of the McElwain Company (R. 108).

As to (b), it is not suggested how "receivership management" could have "intensified" competition. In order to compete, the shoes must be produced and sold at a profit, otherwise losses mount still higher.

To the McElwain officials, who were capable, experienced and deeply interested, the situation "held out no practical opportunity to operate our factories or to conduct our business on a sufficient scale to afford a

reasonable expectation of profit" (R. 579; letter to stockholders quoted above).

As to (c), the record shows that throughout the negotiations the First Preferred stockholders were represented by Mr. James J. Storrow of Lee, Higginson & Co. (R. 300). The contract of sale was, as we have shown, expressly approved by that firm.

The second preferred shares were mostly held by the directors who signed the contract and by the employees of the Company (R. 225).

All the alternatives imagined by the Court of Appeals, and perhaps others, are envisaged in the letter to the stockholders (R. 579) quoted above: "In these circumstances your officers and directors have studied various plans of securing additional capital, all of which have been carefully weighed and analyzed with Messrs. Lee, Higginson & Co., and in conference with our banks."

And all three alternatives can be measured by the actual experience of the business as conducted by the petitioner. It "carried" the McElwain Company, it paid the indebtedness; it took over the property and "kept it in active operation", with the result that from May 31, 1921, (R. 656-7) to November 30, 1921 (R. 657-8) the operating capital of $3,522,418.46 completely disappeared from the balance sheet and the deficit of $4,382,136.70 was increased to the sum of $9,103,076.59.

The experience of the International Shoe Company shows that the McElwain Company's business when operated could not pay its debts, and that the only salvation for all parties in interest was a sale. Since the Federal Trade Commission made its order, repeated efforts to find a purchaser for the property even at a substantial loss, have failed.

(6) It was Error to Test the ability of the McElwain Company to Continue business by the Federal Bankruptcy Definition of Insolvency.

In its Findings (Paragraph 24; R. 532-3) the Commission takes the book value of all the assets (including real estate and plants at approximately $5,000,000) shown on the balance sheets and deducts therefrom the current indebtedness shown, and concludes that "the property of the W. H. McElwain Company * * * "exceeded its debts by" the amount of the remainder. Summarizing the computations thus made the Finding concludes with this:

> "At and prior to the acquisition by respondent (i. e. petitioner here) of the stock or share capital of the W. H. McElwain Company the aggregate of the property of W. H. McElwain Company, at a fair valuation, was more than sufficient in amount to pay its debts. W. H. McElwain was not insolvent prior to the acquisition of its stock or share capital by the respondent, nor subsequent thereto."

Affirming this, the Court of Appeals says: "The Commission expressly found that the McElwain Company was not insolvent within the Bankruptcy Act definition. Plainly it was not".

Both tribunals make this negative finding decisive. Neither tribunal considers the stockholders or the saving of any part of their investment. Both tribunals rest their decision upon the assumption that the debts might be paid. Moreover, the Company's business activity was circumscribed by the law of Massachusetts and by that law the Company's liability to pay its debts as they became due subjected it to involuntary liquidation proceedings for the benefit of creditors,

whether it was insolvent within the meaning of the Bankruptcy Act or not.

For several decades the courts of Massachusetts have held that a trader is insolvent who either has ceased to pay his debts in the ordinary course or cannot pay his debts as they become due. *Thompson v. Thompson* (1849), 4 Cush. 127, 134; *Lee v. Kilburn* (1854), 3 Gray, 594, 600; *Vennard v. McConnell* (1866), 11 Allen, 555, 561; *Peabody v. Knapp* (1891), 153 Mass. 242, 244; *Holbrook v. International Trust Co.* (1915), 220 Mass, 150, 155; *Steele v. Commissioner of Banks* (1922), 240 Mass. 394, 397. And this definition was enacted as a part of the law of sales of personal property. The statutory definition is as follows (General Laws 1921, Chap. 106, Sec. 65 (3)): "A person is insolvent who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due, whether he has committed an act of bankruptcy or not, and whether he is insolvent within the meaning of the federal bankruptcy law or not."

This Court has held that the two definitions of insolvency viz. of the Bankruptcy Act and that by the law of Massachusetts, import different meanings and that each obtains within the realm of the authority enacting it. *United States v. Oklahoma*, 261 U. S. 253, 261.

Neither the Court of Appeals nor the Commission mentions the law of Massachusetts; neither denied the inability of the Company to pay its debts as they became due, neither tribunal explains how the Company's debts could have been paid without the sale of its factories and the discontinuance of the business.

But it is submitted that the true test was solely one of commercial and financial capacity to survive the

embarrassments which confronted the corporation and its management. If the company was doomed in the deliberate and well grounded judgment of its officers and stockholders, then the inhibitions against a sale must cease to operate. The public interest and the avowed purpose of the law could not longer be served by a decision to persist in a hopeless enterprise.

The case of the *American Press Association v. United States,* 245 Fed. 91, was decided by the Court of Appeals for the Seventh Circuit. The situation was this. In 1912 the Government brought suit against the American Press Association, the Western Newspaper Union and others under the Sherman Anti-Trust Act and obtained a decree by which the Western Newspaper Union was permanently enjoined from combining with the American Press Association "either by purchase, stock ownership or in any other manner".

But the circumstances greatly changed. In 1917 the American Press Association was conducting its business at a loss of over $3000 per month and was practically bankrupt. It petitioned the District Court for permission to sell the property as a going concern to the Western Newspaper Union. The District Court denied the petition. The Court of Appeals reversed the decision of the District Court and in the course of its opinion said (page 93):

> "The American Company is forced to go out of the plate business. No decree can stop that. And after the American Company quits, if the Western is left alone in the field, the ultimate situation of the country newspapers would be the same whether the plant be scrapped or sold as an integer. Neither the decree, nor in our judgment, the Sherman Law prevents the Western from buying the scraps piecemeal. If it did buy, it could organize

them anew. If it be permitted to buy the integer, it would save the expense of reorganization. If the plant be scrapped two injuries result; one to the public from the destruction of a usable and useful plant; the other to the stockholders of the American Company."

In the case of *United States v. United States Steel Corporation*, 251 U. S. 417, the Court had before it as one phase the purchase by the defendant of the Tennessee Coal and Iron Company. Concerning this acquisition the Court said (pages 446-7):

"There is, however, an important circumstance in connection with that (i. e. acquisition) of the Tennessee Company which is worthy to be noted. It was submitted to President Roosevelt and he gave it his approval. His approval, of course, did not make it legal, but it gives assurance of its legality, and we know from his earnestness in the public welfare he would have approved of nothing that had even a tendency to its detriment. And he testified he was not deceived and that he believed that 'the Tennessee Coal and Iron people had a property which was almost worthless in their hands, nearly worthless to them, nearly worthless to the communities in which it was situated, and entirely worthless to any financial institution that had the securities the minute that any panic came, and that the only way to give value to it was to put it in the hands of people whose possession of it would be a guaranty that there was value to it'. Such being the emergency, it seems like an extreme accusation to say that the corporation which relieved it, and, perhaps, rescued the company and the communities dependent upon it from disaster, was urged by unworthy motives. Did illegality attach afterwards and how? And what was the corporation to do with the property? Let it decay in desuetude, or develop its capabilities and resources? In the development, of course, there would be profit to the corpora-

tion, but there would be profit as well as to the world. For this reason President Roosevelt sanctioned the purchase and *it would seem a distempered view of purchase and result to regard them as violations of law.*" (Italics ours.)

(7) The evidence in this case makes it clear that the essential purpose which the Clayton Act denounces was absent from the transaction in question. True, the purchase was had by the acquisition of the stock, but that stock was not held, used or voted for the purpose of lessening competition; nor did the ownership of the stock even remotely have such an effect. The aim of the transaction was to save a business that was going on the rocks in the opinion of managers who had been in charge of it for many years. The ownership of the stock was purely formal. The consummation of the purchase of assets was deferred; not because the authority and power of these shares was to be used to influence competition, but because the agreement of the McElwain Company to bring in all shares had not been carried out. The International Shoe Company, wishing to avoid all controversy with a few stockholders who had not come in, postponed the dissolution of the McElwain Company; but in the meantime the control of the assets and the amalgamation of the two properties had in all respects taken place. The effect upon trade was as completely determined as if the assets had been technically transferred before the complaint was filed.

(8) From first to last there is nothing in the procedure and in the consequences of the transaction that invites the denunciation of the law. We submit if this were a proceeding under the Sherman Act, there is no step in the dealings between the parties that would be challenged by any provision of that act as construed by this Court.

The sole question turns upon the particular provision of Section 7 of the Clayton Act. Broadly speaking, there may be a vague competition between all the 1500 concerns engaged in making shoes. To guard against so attenuated a test, the statute requires that only a substantial lessening of competition shall be ground of complaint. We submit that essential competition cannot be based upon the circumstance that at some remote points the trade of the two concerns came in contact, involving nothing more than a negligible number of pairs of shoes. Furthermore, the condition of the McElwain Company was such as to preclude the possibility of any competition then or thereafter.

In all respects the transaction itself was fair, open, without the suggestion of oppression or sinister purpose. So much is admitted by counsel for the Commission (R. 126).

Apart from the question of competition, a transaction otherwise not subject to challenge is attacked solely because the assets were acquired by a purchase of shares. The decisions of this Court make it clear that the mere *purchase of shares does not constitute an offense.*

This Court has said that where the purchase of shares has been followed by the acquisition of title to the assets before the Commission moves, there is no ground for complaint under the Clayton Act, regardless of the question of competition. *Thatcher Manufacturing Co. v. Federal Trade Commission,* 272 U. S. 554. As a means of approach to securing title to assets, the purchase of shares is not improper. In this case, it is true, technically the title to assets was not obtained until after the complaint was filed; and, strictly speaking, such a case has not been passed upon by this Court. But it is also true that in this case the as-

sets of the McElwain Company had been absorbed and, to all intents and purposes, used by petitioner as owner. The two properties were amalgamated and openly used as one for two years before the complaint was filed. Holders of 50 shares of preferred, and 35 shares of common, stock held out, and the formality of passing technical title and the admitted purpose to dissolve the corporation had been delayed. So soon as complaint was made, the technical omission was corrected. The one evil complained of was cured; in the only way in which this could at that stage be done.

Much is made in the record of the manner in which the sale of the stock by the International Shoe Company and the acquisition of assets was effected. We respectfully submit if there was no substantial competition past or prospective this discussion serves no practical purpose. If the company had the right to sell the shares and to acquire the assets, the method adopted does not touch the merits of the transaction.

Should this Court hold that the technical transfer came too late to defeat the complaint, there is still the question of the relief to be ordered. The Commission's order, effective May 7, 1927, (six years after the transaction) calls upon petitioner "to divest itself of the stock of the McElwain Company, and to cease and desist from the ownership, operation and management of the properties formerly owned by the McElwain Company", and this without regard to the $11,000,000 which the International Company advanced to enable the McElwain Company to pay its debts.

It is respectfully submitted that this order is incapable of performance. There are no shares of stock within its control, and there are no takers, if the stock could be offered. So much is obvious. Petitioner would be the only purchaser. The order to desist from the own-

ership and management of the properties cannot be carried out. If petitioner is now the owner (and this the order presupposes), then the general purpose and the technical requirements of the law have been met. If the order contemplates (what it does not say) a resale of the properties, then it can accomplish nothing of practical value, for the obvious reason that they would have to be offered subject to the debts which petitioner now controls. A reinstatement of the situation, it is submitted, embraces debts as well as properties. It stands to reason that purchasers who desisted in the beginning would be more reluctant now to assume such obligations. The financial embarrassment of the concern must deter any outside investor from engaging in it. Only a going concern in immediate and peculiar need of the facilities offered, and prepared to pay correspondingly for them what no one else could be induced to give, would consider the proposition. This is the sole explanation for the prompt purchase by petitioner at a price that advantageously salvaged the properties for all concerned, instead of waiting to take them at ruinous figures after the inevitable crash. It has not been possible to secure any offers for the assets and it must be apparent that at any sale the petitioner would be the only bidder. The result would be that the title which it now holds would be confirmed.

Respectfully submitted,

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